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114737—36——1

In the Supreme Court of the United States

OCTOBER TERM, 1936

No. 331

UNITED STATES OF AMERICA, PETITIONER

v.

A. B. LEACH & CO., INC.

ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SEVENTH CIRCUIT

BRIEF FOR THE UNITED STATES

OPINIONS BELOW

The opinion of the District Court (R. 5) is not officially reported. The opinion of the Circuit Court of Appeals (R. 15–17) is reported in 84 F. (2d) 908.

JURISDICTION

The judgment of the Circuit Court of Appeals was entered June 30, 1936 (R. 18). The petition for a writ of certiorari was filed September 1, 1936, and was granted October 19, 1936. The jurisdiction of this Court rests on Section 240 (a) of the Judicial Code, as amended by the Act of February 13, 1925.

QUESTION PRESENTED

Respondent subscribed for the original shares in several corporations it organized. The shares were then issued in the name of an employee of respondent, appointed to receive and hold them for respondent's benefit and convenience in connection with future sales thereof to the public. Did this transaction involve a taxable transfer by respondent, within the purview of Section 800, Schedule A–3 of the Revenue Act of 1926?

STATUTES AND REGULATIONS INVOLVED

These are set forth in the Appendix, *infra*, pp. 15–18.

STATEMENT

This action was brought by respondent on September 11, 1933, for the recovery of $16,526.40 paid as documentary stamp taxes. (R. 1–5). Petitioner filed a general demurrer to respondent's declaration and the District Court on July 16, 1935, entered its memorandum opinion wherein it concluded that respondent should recover (R. 5). Petitioner elected to stand on its demurrer and, accordingly, on November 22, 1935, the court entered judgment in favor of respondent and against petitioner for $16,526.40, with interest, and allowed petitioner an exception (R. 6). On December 3, 1935, petitioner filed written exceptions to the order of judgment and refusal and failure of the court to sustain petitioner's demurrer (R. 6–8)

and, on December 5, 1935, moved to vacate the judgment (R. 8–9), which motion was overruled forthwith and an exception allowed (R. 14). On appeal the Circuit Court of Appeals affirmed the judgment (R. 17, 18).

The facts, as set forth in respondent's declaration (R. 1–5), may be summarized as follows:

Respondent is a corporation organized under the laws of New York and, from July, 1917, to April, 1932, was engaged in the sale of securities to the public (R. 1). Prior to September, 1931, but subsequent to enactment of the Revenue Act of 1926, respondent organized five corporations and subscribed for all of their original issue stock, aggregating 826,320 shares (R. 1–3). Immediately upon completion of the organization of the corporations, the stock so subscribed for was issued in the name of one Vercouter, an employee of respondent appointed to receive and hold the capital stock of the corporations for respondent's benefit and convenience in connection with future sales and transfers of the stock to the public (R. 3–4). The original issue tax of five cents on each share was paid as required under Schedule A–2, Title VIII of the Revenue Act of 1926, and is not in dispute.

In August and September, 1931, the Commissioner of Internal Revenue assessed transfer taxes against respondent in the aggregate sum of $16,526.40, under Schedule A–3 of said Act, in respect of the foregoing transactions (R. 1–3), upon the

transfer by respondent of its right to receive said stock.

The assessments were paid and, on October 8, 1932 (R. 4), respondent filed claims for refund which were denied by the Commissioner on March 18, 1933, on the ground that respondent (R. 4–5)—

> * * * subscribed for the stock involved and directed that it be issued in the name of its nominee; that the nominee therefore received the legal title to the stock which petitioner [respondent] had the right to receive and such transfer of the right to receive is subject to the tax, * * *.

SPECIFICATION OF ERRORS TO BE URGED

The Circuit Court of Appeals erred:

1. In failing to hold that the transactions involved constituted transfers by respondent to its nominee of the right to receive shares of stock within the stamp tax provisions of the Revenue Act of 1926.

2. In holding that the transactions involved were not subject to the transfer stamp tax provisions of the Revenue Act of 1926.

3. In affirming the judgment of the District Court.

SUMMARY OF ARGUMENT

Respondent, as sole subscriber to the shares of five newly organized corporations, had the right to receive those shares and the right to command their disposition. Respondent's direction to the issuing

corporations that the stock and certificates be issued in the name of its employee, Vercouter, called the statute into operation. The subsequent act of issuance effectively completed the transfer of respondent's right to receive the shares. The decision of the court below holding that no taxable transfer was effected is inconsistent with the decision of this Court in *Raybestos-Manhattan Co.* v. *United States*, 296 U. S. 60. The fact that in that case a beneficial interest was transferred, whereas here the transferee secured no beneficial interest, is immaterial under the statute and regulations. This was pointed out by the Circuit Court of Appeals for the Second Circuit in *Founders General Corporation* v. *Hoey*, 84 F. (2d) 976, pending on writ of certiorari, No. 398.

Amendments to the Act of 1926 reinforce the conclusion that nominee transactions fall within the scope of the stamp tax provisions. The Revenue Act of 1932 exempted certain transfers or deliveries by a fiduciary to a nominee, or by one nominee of a fiduciary to another. An amendment enacted on June 29, 1936, exempts certain transfers or deliveries by or to nominees of brokers. These specific exceptions are not applicable in the present case, since respondent acted neither as fiduciary nor as broker, and since the 1926 Act applies. But their enactment demonstrates that nominee transactions of the type here involved are intended to be covered by the general provisions of the statute.

ARGUMENT

Section 800, Schedule A–2 of the Revenue Act of 1926, *infra*, imposes a stamp tax at a specified rate on the original issue of shares of corporate stock. By Section 800, Schedule A–3, *infra*, a like tax is laid—

> On all sales, or agreements to sell, or memoranda of sales or deliveries of, or transfers of legal title to shares or certificates of stock * * *, or to rights to subscribe for or to receive such shares or certificates, whether made upon or shown by the books of the corporation, * * *, or by any paper or agreement or memorandum or other evidence of transfer or sale, *whether entitling the holder in any manner to the benefit of such stock, interest, or rights, or not,* * * *. [Italics supplied.]

Section 800 imposes liability for the tax upon the transferor, the transferee or the corporation whose stock is transferred. *Raybestos-Manhattan Co.* v. *United States,* 296 U. S. 60.

Respondent corporation was engaged in the business of selling securities to the public. It organized five corporations for all of whose original issues of stock it subscribed. Immediately on the completion of the organization of said corporations, the stock so subscribed for was issued, pursuant to respondent's direction, in the name of its agent and employee, one Vercouter, "appointed to receive and hold" the stock for respondent's benefit

and convenience in connection with contemplated sales and transfers to the public. (R. 3–4).

Respondent contends that its subscriptions to the stock and the issuance thereof in the name of Vercouter, pursuant to its direction, constituted a single transaction, taxable only under Schedule A–2 relating to the original issue, and that Schedule A–3 has no application. This contention, we submit, overlooks the essential character of the transaction and unduly restricts the scope of the taxing Act.

The respondent, as sole subscriber to the shares of the newly formed corporations had the right to receive the shares for which it subscribed. Respondent necessarily had the right to command the disposition of the shares, including the right to direct the issuance of the stock to another. Respondent's direction to the corporations to issue the stock and certificates in the name of Vercouter called the statute into operation. If the nomination of Vercouter is insufficient, of itself, to effect a taxable transfer of respondent's right to receive, the subsequent act of issuance effectively completed the transfer of that right and clearly brought the taxing statute into operation.

The transaction was not merely one of form. There was a transfer in substance as well. Upon issuance of the stock certificates in the name of Vercouter, legal title to the stock was vested in him and he doubtless appeared on the books of the issu-

ing corporations as a stockholder. Consequently, respondent could not thereafter have caused the transfer of the stock to purchasers, nor could respondent have transferred the certificates therefor, without appropriate endorsement by Vercouter.

Respondent's right to receive the stock and legal title thereto was as effectively transferred by the method followed as if the stock had first been issued to respondent as subscriber and then endorsed and surrendered with directions to reissue in the name of Vercouter. The fact that respondent could perhaps have withdrawn its direction to the issuing corporation becomes unimportant upon actual issuance of the stock pursuant to the direction given by respondent and not withdrawn.

When thus viewed, we submit, the transaction involved a taxable transfer by respondent within the scope of the statute as described by this Court in *Raybestos-Manhattan Co.* v. *United States,* 296 U. S. 60, 62.

> The stock transfer tax is a revenue measure exclusively. Its language discloses the general purpose to tax every transaction whereby the right to be or become a shareholder of a corporation or to receive any certificate of any interest in its property is surrendered by one and vested in another. See *Provost* v. *United States,* 269 U. S. 443, 458, 459. While the statute speaks of transfers, it does not require that the transfer shall be directly from the hand of the transferor to that of the transferee. It is

> enough if the right or interest transferred is, by any form of procedure, relinquished by one and vested in another.

It may be true that as between respondent and Vercouter the latter had no beneficial interest in the shares. Such an interest, however, is not requisite to liability for the tax. The statute taxes a transfer even though the holder is not entitled "in any manner to the benefit of such stock, interest, or rights". (*Infra*, p. 16.) Treasury Regulations 71, Article 34 (u) similarly provide that "Transfers of stock are subject to the tax even though the holders thereof are not entitled in any manner to the benefit of the stock". (*Infra*, p. 18.)

The court below apparently gave controlling weight to the fact that what was transferred by respondent was not a beneficial interest such as was involved in the *Raybestos-Manhattan* case, *supra*. (R. 17.) In so deciding the court followed a decision of a District Court in *Union Trust Company* v. *Heiner*, 26 F. (2d) 391 (W. D. Pa.), which in turn has been followed in several other cases in the Seventh Circuit and elsewhere.[1] The reasoning of the court in the *Union Trust Company* case was

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[1] *Field, Glore & Co.* v. *United States* (N. D. Ill.), decided April 8, 1935, not officially reported but found in Vol. I, Prentice-Hall, 1935, par. 1196; *id.*, par. 1197; *Lawrence Stern & Co.* v. *United States* (N. D. Ill), decided July 17, 1935, not officially reported but found in Vol. I, Prentice-Hall, 1935, par. 1947. See also *White* v. *Consolidated Equities*, 78 F. (2d) 435 (C. C. A. 1st), and *Dean* v. *Caldwell & Co.*, 9 F. Supp. 177 (M. D. Tenn.).

expressly rejected by the Circuit Court of Appeals for the Second Circuit in *Founders General Corporation* v. *Hoey*, 84 F. (2d) 976, now pending on writ of certiorari, No. 398. In that case Judge A. N. Hand said (p. 978):

> It is plain that the court in *Union Trust Company* v. *Heiner* ignored the express provision that the absence of any beneficial interest on the part of the holder should not exempt the transfer from taxation. The decision, therefore, proceeded on an indefensible theory. That decision has since been followed by various district courts, but we cannot avoid the conclusion that it is contrary to the plain meaning of the statute.

The decision of the court below has the effect of enlarging the class of exemptions prescribed by the statute. Schedule A-3 of the 1926 Act exempts transfers of the following kinds: Transfers of stock as collateral security for money loaned; transfers to a broker for sale; and transfers from a broker to a customer upon whose order he has made the purchase. The specific exemption of these classes of transfers strongly indicates that Congress intended to exclude all other kinds of transfers from the exempted class. *Cf. George A. Hormel & Co.* v. *United States*, 10 F. Supp. 623, 625 (D. Minn.); *Founders General Corp.* v. *Hoey*, *supra*, at 979.

Amendments subsequent to the 1926 Act confirm the conclusion set forth above. Section 723 of the

Revenue Act of 1932, c. 209, 47 Stat. 273, added the following proviso:

> Provided further, That the tax shall not be imposed upon deliveries or transfers from a fiduciary to a nominee of such fiduciary, or from one nominee of such fiduciary to another, if such shares or certificates continue to be held by such nominee for the same purpose for which they would be held if retained by such fiduciary, or from the nominee to such fiduciary, but such deliveries or transfers shall be accompanied by a certificate setting forth the facts:

It will be observed that this proviso granted an exemption in the case of certain nominee transactions, but that the exemption was strictly limited to transfers from a fiduciary to his nominee or from one nominee of a fiduciary to another, and it was required that a certificate setting forth the facts accompany the delivery or transfer. The inference is plain that had Congress intended to exempt nominee transactions generally a different provision would have been employed. It is equally clear that, in the absence of such a specific exemption, nominee transactions were intended to be included in the general class of taxable transfers. *Cf. Gooch* v. *United States,* 297 U. S. 124, 129.

Again, in 1936, a significant amendment was adopted. Act of June 29, 1936, c. 865, 49 Stat. 2029. Previously, deliveries or transfers to a broker for sale, or by a broker to a customer

upon whose order securities were purchased, were exempted from tax. The 1936 amendment extended that exemption to include transfers to or by a registered nominee of a broker. The amended provision follows, with the new material indicated by italics:

> *Provided further,* That the tax shall not be imposed upon deliveries or transfers to a broker *or his registered nominee* for sale, nor upon deliveries or transfers by a broker *or his registered nominee* to a customer for whom and upon whose order [he] *the broker* has purchased same, *nor upon deliveries or transfers by a purchasing broker to his registered nominee if the shares or certificates so delivered or transferred are to be held by such nominee for the same purpose as if held by the broker,* but such deliveries or transfers shall be accompanied by a certificate setting forth the facts: * * *

The respondent suggests (Brief in Opposition, p. 6) that the 1936 amendment is applicable to the situation involved in the present case. There are two short answers to this suggestion: First, the provision is not retroactive, but applies only to transfers executed subsequently thereto. Treasury Regulations 71, Article 35, have been specifically amended to conform to the 1936 statutory change; and the amendment is expressly limited to deliveries or transfers occurring on or after June 29, 1936. See Cum. Bul. XV–43 p. 15. Second, the

new provision applies only to brokerage transactions. The facts in the instant case indicate that respondent was engaged as a dealer in securities purchasing for its own account and not as a broker purchasing for the account of a customer.

While the 1936 amendment does not apply to the instant case, its enactment, like that of the 1932 amendment, is of significance. Congress has exempted a somewhat larger class of nominee transactions than previously, but has not deemed it advisable to exempt nominee transactions generally. In adopting the 1936 amendment, Congress acted upon the assurance that the desired result could not be achieved by a change in the Treasury Regulations.[2] The contentions of respondent are thus seen to be an effort to read into the stamp tax provisions an exception which Congress has not seen fit to make.

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[2] The Report of the House Committee on Ways and Means indicates that the amendment was proposed in order to place corporate brokers upon an equality with unincorporated brokers, since the former have felt compelled to take delivery of shares in the name of an individual. The Report states: "This committee believes that such discrimination is unjust and inequitable, and is assured that such discrimination cannot be removed by a change in Treasury Department regulations, but that the enactment of this bill is necessary to overcome the inequality." House Report 3023, 74th Cong., 2d Sess., p. 2.

CONCLUSION

For the reasons stated the judgment of the Circuit Court of Appeals should be reversed.

Respectfully submitted.

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DECEMBER 1936.

APPENDIX

Revenue Act of 1926, c. 27, 44 Stat. 9, 99, 101:

TITLE VIII. STAMP TAXES

SEC. 800. On and after the expiration of thirty days after the enactment of this Act there shall be levied, collected, and paid, for and in respect of the several bonds, debentures, or certificates of stock and of indebtedness, and other documents, instruments, matters, and things mentioned and described in Schedule A of this title * * *. (U. S. C., Title 26, Sec. 900.)

SCHEDULE A. STAMP TAXES

* * * * *

2. Capital stock, issue: On each original issue, whether on organization or reorganization, of certificates of stock, or of profits, or of interest in property or accumulations, by any corporation, on each $100 of face value or fraction thereof, 5 cents: *Provided,* That where a certificate is issued without face value, the tax shall be 5 cents per share, unless the actual value is in excess of $100 per share, in which case the tax shall be 5 cents on each $100 of actual value or fraction thereof, or unless the actual value is less than $100 per share, in which case the tax shall be 1 cent on each $20 of actual value, or fraction thereof.

The stamps representing the tax imposed by this subdivision shall be attached to the stock books and not to the certificates issued.

3. Capital stock, sales or transfers: On all sales, or agreements to sell, or memoranda of sales or deliveries of, or transfers of legal title to shares or certificates of stock or of profits or of interest in property or accumulations in any corporation, or to rights to subscribe for or to receive such shares or certificates, whether made upon or shown by the books of the corporation, or by any assignment in blank, or by any delivery, or by any paper or agreement or memorandum or other evidence of transfer or sale, whether entitling the holder in any manner to the benefit of such stock, interest, or rights, or not, on each $100 of face value or fraction thereof, 2 cents, and where such shares are without par or face value, the tax shall be 2 cents on the transfer or sale or agreement to sell on each share: *Provided,* That it is not intended by this title to impose a tax upon an agreement evidencing a deposit of certificates as collateral security for money loaned thereon, which certificates are not actually sold, nor upon the delivery or transfer for such purpose of certificates so deposited, nor upon mere loans of stock nor upon the return of stock so loaned: *Provided further,* That the tax shall not be imposed upon deliveries or transfers to a broker for sale, nor upon deliveries or transfers by a broker to a customer for whom and upon whose order he has purchased same, but such deliveries or transfers shall be accompanied by a certificate setting forth the facts: *Provided further,* That in case of sale where the evidence of transfer is shown only by the books of the corporation the stamp shall be placed upon such books; and where the change of ownership is by transfer of the certificate

the stamp shall be placed upon the certificate; and in cases of an agreement to sell or where the transfer is by delivery of the certificate assigned in blank there shall be made and delivered by the seller to the buyer a bill or memorandum of such sale, to which the stamp shall be affixed; and every bill or memorandum of sale or agreement to sell before mentioned shall show the date thereof, the name of the seller, the amount of the sale, and the matter or thing to which it refers. Any person liable to pay the tax as herein provided, or anyone who acts in the matter as agent or broker for such person, who makes any such sale, or who in pursuance of any such sale delivers any certificate or evidence of the sale of any stock, interest or right, or bill or memorandum thereof, as herein required, without having the proper stamps affixed thereto, with intent to evade the foregoing provisions, shall be deemed guilty of a misdemeanor, and upon conviction thereof shall pay a fine of not exceeding $1,000, or be imprisoned not more than six months, or both. (U. S. C., Title 26, Sec. 902.)

Treasury Regulations 71, approved July 7, 1928, promulgated under the Revenue Act of 1926:

ART. 31. *Basis of tax.*—Every transfer or sale of stock, either before or after issuance of a certificate, is taxable. The tax accrues at time of making the sale or agreement to sell or memorandum of sale, or delivery of, or transfer of the legal title to shares, or certificates of stock, or of profits, or of interest in property or accumulations in any corporation, joint-stock company, or association, or of the right to subscribe for or

to receive such shares or certificates, regardless of the time or manner of the delivery of the certificate or agreement or memorandum of sale.

ART. 34. *Sales and transfers subject to tax.*—The following transactions are subject to the tax:

(a) The sale, or transfer, or change of ownership, of certificates of stock, or of profits, or of interest in property or accumulations in corporations, joint-stock companies, or associations.

(b) The sale or transfer of shares of stock, whether or not represented by certificates.

(c) The transfer of stock to or by trustees.

* * * * *

(g) The transfer of the interest of a subscriber for stock, however such interest may be evidenced or conditioned upon further payments.

(h) The transfer of the right to subscribe for stock in any corporation, joint-stock company, or association, whether or not evidenced by warrants.

* * * * *

(t) The transfer of the right to receive stock which a corporation has unconditionally agreed to issue.

(u) Transfers of stock are subject to the tax even though the holders thereof are not entitled in any manner to the benefit of the stock.

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